Idea tools and techniques

Do you have a great business idea? Do you want to start your business, but you are short of funds? How do you put ideas into action and how do you implement those actions? Are the finances the only thing needed? How much money can and should be raised, when and from whom? New entrepreneurs are often faced with many challenging questions about financing once they develop a business plan.

After completing this module, you will be able to describe typical financing strategies across different phases of the company lifecycle and understand the benefits and risks associated with different funding options. Getting from an idea to an actual business.

Entrepreneurship and Entrepreneurial Finance: an overview

Entrepreneurship

Before we delve into the study of entrepreneurial finance, let's define what we mean by entrepreneurship and finance.

The term entrepreneurship is derived from the French word 'Entreprendre', which means to undertake, pursue opportunities, or fulfill needs and wants through innovation and starting businesses[1]. The term first appeared in the French dictionary back in 1723. There is no universally agreed definition of entrepreneurship as the concept is understood differently by different scholars and authors and as it evolves with time.

Entrepreneurship can be defined as the process by which individuals pursue opportunities without regard to resources they currently control for the purpose of exploiting future goods and services. Others define entrepreneurship as the art of turning an idea into a business[2]. In this course, we focus on entrepreneurship in the context of an entrepreneur launching a new business.

There are many misconceptions about who entrepreneurs are and what motivates them to launch firms to develop their ideas and this is due to the fact that most of the society works full-time and does not know the realities of business.

Which entrepreneurship myths are most common[3]?

1. You need to wait for the right time

"This is not the best time…" - this is exactly how many of us justify postponing the decision to start our own business. We have too little capital, too little time, we don't have a plan. If we really want to run our own business, every moment to open a company is good. Take small steps, and prepare as much as you can.

2. You need to know everything

To start your own business you don't need to know everything, you just need to be open to new ideas and different approaches to your business. In order to succeed you will need to be flexible and have good planning and organizational skills.

3. You need to be a risk-taker

Acceptance of risk is in a way inscribed in the entrepreneur's DNA. There is no business without risk, although it can be gradually reduced by gaining experience and learning from someone else's or your mistakes.

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[1] Sobel R., Entrepreneurship https://www.econlib.org/library/Enc/Entrepreneurship.html

[2] Barringer B., Ireland R,. (2019) "Entrepreneurship: Successfully Launching New Ventures", p.32.

[3] Castrillon C., 5 Common Myths About Entrepreneurship Debunked

4. You need a huge budget

It all depends on the type of business you want to open. If you dream of a fine dining restaurant in a good neighborhood, you need a lot of capital. However, most of the first businesses do not require great investment, especially if the main capital is your skills or other things you already have. In the next modules of this course, you will learn more about sources of financing your business.

How to think like an entrepreneur? Watch the presentation of Amy Wilkinson who reveals the key to becoming a successful entrepreneur:

The Secret of How to Think Like an Entrepreneur | Amy Wilkinson | TEDxPaloAltoSalon

Entrepreneurial Finance

Another big word that will accompany us in this course is finance.

Entrepreneurial finance is defined as the set of activities such as the application and adaptation of financial tools, techniques and principles carried out by entrepreneurs to secure and manage funds. These activities are based on the study and analysis of the needs for starting and operating the new venture[4]. New ventures differ from established enterprises, so the decisions they face, especially finance decisions vary.

Sources of entrepreneurial financing

To start with the financial part, where in most cases you will be looking for investors to support you, you need to ask yourself a question: what do I invest? Did you hear about sweat equity? To put it in simple words, it is your time and money and effort that you put into your startup and we shall underline a passion in here. If you are not passionate enough about something you want to do, how can it work out then? It's simple – if you are not going to invest your sweat equity, you can't expect investors to invest their money, time and efforts.

So, if you make sure that your sweat equity is fully invested, what are the sources to finance your entrepreneurship? Everybody talks about venture capital and business angels, or even groups of angels that sometimes ask very much like VC. In the next

[4] Da Rin M., Hellmann T., (2020) "Fundamentals of Entrepreneurial Finance", pp. 1-3.

modules we will take a closer look into business angels and VC worlds. What else is in there? Banks, if you can take out a loan or credit. Grants, depending on where you want to start your business and what exactly do you need money for. Lastly, you also have the option of customers & vendors.

How to choose the best possible financial option for your business? Three things should be taken into consideration:

1. Consequences of failure – what are the consequences of failure of your business from your investor's perspective. The options can be different, depending if your plan is excellent and investors see that from the beginning or your plan requires high risk financial help.

2. Investment amount – depending on the amount of money you need, you should consider what different financial options offer to you and match them with your needs.

3. Investment timing – simple rule "the younger you are, the riskier you are" tells enough in this topic and keep in mind that if you are a beginner entrepreneur, some sources of entrepreneurial finance may be not available for you. In any case, there are always some options.[5]

Let's move then to an overview of thirteen typical sources of entrepreneurial finance.

1. The founders – it is basically your capital; how much money you can invest in your own startup. Maybe you have some savings, you won in a lottery or you received a bonus at work?

2. The 3Fs – this abbreviation stands for Family, Friends and Fools. Before you start looking for investors, look around in your own circle. Maybe you have a rich uncle who is ready to support your business? Or do your friends believe in your success so much that they will support you with some sum of money for a good start? Where are the fools in this? Well, if you are a beginner entrepreneur your 3Fs take quite a big risk investing their money, but someone with a little bit knowledge of the world of business knows how sometimes you have to be the brave and the bold one to succeed. Without a little bit of risk it's difficult to achieve big things.

3. Business angels – usually they are experienced entrepreneurs who invest their own capital in your startup. The world angel is very much connected

[5] Entrepreneurial Finance Module 4

with their role – the experienced one is taking the unexperienced under their wings and guiding them in the process, not only with money support but very often with mentoring as well.

4. Crowdfunding – literally, it is the crowd that gathers money to support some business idea. Usually it takes place on online platforms, where people can make money transfers for a startup they support.

5. Subsidies – look around you, there are always some subsidies to support you on any stage of your business, either on regional, country or European level.

6. Venture capital/private equity – there are many professional investment firms operating with big capitals. Specifically, VC focuses mainly on risky investments in companies that are on their early stages of development.

7. Debt financing: the bank – banks invest mostly in lower risk startups and the good thing about them is that while investing in you they do not take shares of your business.

8. Factoring – instead of receiving money for the invoice from individual clients, you can decide to receive it from a special factoring company; in this case you need to be eligible for factoring, thus to have clients.

9. Leasing – if your business requires investing in some assets, for example computers, but doesn't have capital to purchase them, why not go with leasing instead?

10. Suppliers – negotiate with your suppliers, you can always agree on some favorable payment terms.

11. Initial Coin Offering (ICO) – when you pitch your idea and you ask the general audience to finance your startup with bitcoin or other cryptocurrencies.

12. Initial public offering (IPO) – before going public your business is private, but by offering it to the public you invite them to buy shares of your company.

13. Revenue based financing – the investor supports your business with capital and in return asks to receive an agreed percentage of revenues that your business will generate in the future.[6]

It is always good to do some research about all possible ways of financing and to understand which way will be the best for your business specifically. In the next modules we will take under magnifying glass business angels and venture capital.

When still in doubt, get inspired and watch:

Startup Funding Explained: Everything You Need to Know

[6] Thirteen sources of finance for entrepreneurs: make sure you pick the right one! | EY